No. 06-937

In the Supreme Court of the United States

QUANTA COMPUTER, INC., ET AL., PETITIONERS

v.

LG ELECTRONICS, INC.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONERS

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QUESTION PRESENTED

Whether a patentee, having authorized the sale of the particular article at issue, can nonetheless invoke patent law to remedy a violation of a purported restriction on the purchaser's right to use the article for its only reasonable use.

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INTEREST OF THE UNITED STATES

This case presents the question whether a patentee, having authorized the sale of an article, can nonetheless invoke the patent laws to remedy a violation of a purported restriction on the purchaser's right to use the purchased article for its only reasonable use. The United States Patent and Trademark Office, which is responsible for issuing patents and advising the President on issues of patent policy, 35 U.S.C. 2(a)(1) and (b)(8), has a substantial interest in the resolution of that question. Moreover, because the scope of, and uncertainty over, patent rights may directly affect competition and innovation in the marketplace, this case implicates questions of core concern to the Antitrust Division of the United States Department of Justice. At the invi-

tation of the Court, the United States filed a brief as amicus curiae at the petition stage.

STATEMENT

1. Respondent owns several patents that relate to systems and methods for receiving and transmitting data in computer systems. Pet. App. 2a. Petitioners are manufacturers who build computer systems by combining computer parts with specialized microprocessors and chipsets purchased from Intel Corporation. *Id.* at 2a, 29a-30a. Intel is authorized by a cross-license agreement (License) with respondent to manufacture, and to sell to petitioners, those specialized components, which allegedly meet many of the limitations of respondent's patents. *Id.* at 2a-3a, 29a-30a, 33a-34a, 45a-46a, 55a.

The License authorizes Intel to "make, use, sell (directly or indirectly), offer to sell, import and otherwise dispose of all Intel Licensed Products." Pet. App. 33a (citation omitted).[1] The License expressly disclaims any express or implied license for acts of infringement that may occur when a third party—such as petitioners—combines Intel components with non-Intel components. Br. in Opp. 4-5 (citing License § 3.8). A contemporaneous Master Agreement that incorporates the License by reference also provides that respondent's "grant of a license to Intel for Integrated Circuits . . . shall not create any express or implied license under [respondent's] patents to computer system makers that combine Intel Integrated Circuits with other non-Intel components." *Id.* at 6 (quoting Master Agreement § 2). The

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[1] Apart from the portions quoted in the opinions and by the parties, the provisions of the relevant agreements are confidential. See Br. in Opp. 4 n.1. The United States does not have access to those agreements.

License, however, also states: "Notwithstanding anything to the contrary in this Agreement, the parties agree that nothing herein shall in any way limit or alter the effect of patent exhaustion that would otherwise apply when a party hereto sells any of its Licensed Products." *Id.* at 5 (quoting License § 3.8) (emphases omitted).

The Master Agreement provides that Intel will send a notice to its customers stating that Intel has a "broad patent license" from respondent that "ensures that any Intel product that you purchase is licensed by [respondent] and thus does not infringe any patent held by [respondent]." Br. in Opp. 7 (quoting Attachment C). The notice further states: "*Please note however that while the patent license that [respondent] granted to Intel covers Intel's products, it does not extend, expressly or by implication, to any product that you may make by combining an Intel product with any non-Intel product.*" *Ibid.* Petitioners received that notice from Intel before purchasing some of the components at issue. See *ibid.*; Reply Br. 9.

2. Respondent sued petitioners for patent infringement. Pet. App. 30a. Respondent did "not contend that the Intel microprocessors and chipsets, alone, infringe any of the patents at issue." *Ibid.* Rather, it alleged that "the licensed Intel products meet many of the limitations of the patents and, when combined with other components in the accused devices, infringe five of its patents." *Ibid.*

Relying on *United States* v. *Univis Lens Co.*, 316 U.S. 241 (1942), the district court held that respondent's patent claims were barred by the patent-exhaustion doctrine. Pet. App. 26a-51a. Having "licensed to Intel the right to practice [its] patents and sell products embody-

ing its patents," respondent could not assert an infringement claim "against those who legitimately purchase and use the Intel microprocessor and chipset." *Id.* at 33a. The court emphasized that the components purchased by petitioners from Intel include elements of respondent's patents and have no reasonable use except in the practice of respondent's patents. *Id.* at 32a-49a; see *id.* at 55a.

In a subsequent order (Pet. App. 52a-61a), the court rejected respondent's argument that the patent-exhaustion doctrine did not apply because Intel "expressly informed [petitioners] that their purchase of components from Intel did not grant them a license to infringe [respondent's] patents." *Id.* at 58a. The district court reasoned that, notwithstanding the notice, petitioners' purchase was "unconditional, in that [petitioners'] purchase * * * was in no way conditioned on their agreement not to combine the Intel microprocessors and chipsets with other non-Intel parts and then sell the resultant products." *Ibid.*

The district court also held, however, that the *method* claims in respondent's patents were not subject to exhaustion. Pet. App. 60a. The court further held that petitioners did not acquire an implied license "because Intel expressly disclaimed the existence of such a license." *Id.* at 61a.

3. The court of appeals reversed the district court's judgment that respondent's system claims were exhausted. Pet. App. 1a-25a. The court reasoned that the patent-exhaustion doctrine is triggered only by an "unconditional" sale because, in such a transaction, the patentee "has bargained for, and received, an amount equal to the full value of the goods." *Id.* at 4a-5a (citation omitted). By contrast, in an "expressly conditional sale

or license," the court explained, "it is more reasonable to infer that the parties negotiated a price that reflects only the value of the 'use' rights conferred by the patentee." *Id.* at 5a (citation omitted).

Here, the court concluded that Intel's sales to petitioners were "conditional." Pet. App. 6a. The court pointed to the License, which "expressly disclaims granting a license allowing computer system manufacturers to combine Intel's licensed parts with other non-Intel components" and "required Intel to notify its customers of the limited scope of the license, which it did." *Ibid.* Thus, the court concluded that, "[a]lthough Intel was free to sell its microprocessors and chipsets, those sales were conditional, and Intel's customers were expressly prohibited from infringing [respondent's] combination patents." *Ibid.*

The court affirmed the district court's holding that respondent's method claims were not exhausted, on the ground that there was no unconditional sale. Pet. App. 6a. In the alternative, the court held that "the sale of a device does not exhaust a patentee's rights in its method claims." *Ibid.*

SUMMARY OF ARGUMENT

I. Since at least 1853, this Court has held that a patentee's (or authorized licensee's) sale of an article embodying the patentee's invention frees that particular article from any further patent-law restrictions on its use or resale. Restrictions on downstream use or resale may arise as a matter of state contract law, but not patent law; in acquiring valid title to the article, the purchaser also acquires the right to use and to sell it without fear of patent-infringement claims by the patentee. That understanding of the scope of the patent rights

afforded patentees under the patent law is known as the patent-exhaustion or first-sale doctrine, and is derived from the text and history of the patent statute, the purposes of patent law, and the adverse practical consequences of an alternative rule.

II. In recent years, the first-sale doctrine has evolved in the Federal Circuit in a manner that is at odds with this Court's precedents. Under the Federal Circuit's approach, the doctrine is merely a default rule that is overridden whenever a patentee chooses to impose explicit unilateral or bilateral restrictions on the rights of purchasers to use or to sell the patented article. Such restrictions (with certain limitations derived from antitrust or other law) are enforceable against all downstream users in a patent-infringement suit. That approach is irreconcilable with this Court's cases, which make clear that the patent-exhaustion doctrine applies despite explicit restrictions imposed by the patentee. *E.g.*, *United States* v. *Univis Lens Co.*, 316 U.S. 241 (1942).

The Federal Circuit's approach to the first-sale doctrine rests on the mistaken premises that (1) for patent-exhaustion purposes, a "conditional" sale includes an authorized sale where title passes but the patentee has purported to impose restrictions on use or resale by downstream purchasers, and (2) the patentee can enforce such restrictions through a patent-infringement suit without regard to the patent-exhaustion doctrine. Those premises are inconsistent with this Court's cases.

III. This Court should not follow the Federal Circuit's lead and transform a long-standing substantive limitation on patent rights into a default rule applicable only when the patentee fails to impose explicit restrictions on the rights acquired by purchasers in authorized

sales. The patent-exhaustion doctrine is grounded in sound doctrinal and policy reasons. The inconvenience and inefficiency of the Federal Circuit's approach could extend the entire length of a product's distribution chain, and could enable patentees to demand and obtain royalties beyond those that the statute was intended to provide. That approach also gives inadequate scope to the antitrust laws. With regard to post-sale limitations on the right to use or to sell, a patentee-seller should be placed in no better position with respect to the antitrust laws than any other seller.

IV. The judgment below rests on an erroneous understanding of the patent-exhaustion doctrine. Because the court of appeals did not determine whether Intel's authorized sales to petitioners resulted in exhaustion of the relevant patents under the appropriate standard, vacatur and remand are appropriate.

ARGUMENT

This Court first enunciated the doctrine of patent exhaustion, also known as the first-sale doctrine, more than 150 years ago as a limitation on the exclusive rights conferred under the patent laws. The doctrine bars the use of patent law (but not contract law) to enforce restrictions on a purchaser's use or resale of a patented article that was purchased from the patentee or from someone authorized by the patentee to sell the article. With but a single, short-lived exception, the Court has adhered to that understanding of the doctrine in all of its subsequent decisions. In recent years, however, the Federal Circuit has downgraded the rule to a default presumption, subject to override at the option of the patentee. The decision below rests on that understanding of patent exhaustion, which cannot be reconciled

with this Court's decisions. This Court should adhere to its precedents and reject the diluted version of the patent-exhaustion doctrine on which the decision below is premised.

I. UNDER THIS COURT'S CASES, THE PATENT-EXHAUSTION DOCTRINE DELIMITS THE EXCLUSIVE RIGHTS GRANTED BY PATENT LAW

A. After An Authorized Sale Of An Article Embodying The Invention, A Patentee Cannot Enforce Restrictions On Use Or Resale By Means Of Patent Law

The patent law grants to the patent-holder the "right to exclude others from making, using, offering for sale, or selling the invention." 35 U.S.C. 154(a). Since *Bloomer* v. *McQuewan*, 55 U.S. (14 How.) 539 (1853), this Court has repeatedly made clear that the exclusive rights to use or to sell are exhausted, as to a given article embodying the invention, upon the first valid sale of the article by the patentee or an authorized licensee. *Id.* at 549-550; see, *e.g.*, *Aro Mfg. Co.* v. *Convertible Top Replacement Co.*, 377 U.S. 476, 497 (1964) (plurality opinion); *Univis*, 316 U.S. at 251-252; *Motion Picture Patents Co.* v. *Universal Film Mfg. Co.*, 243 U.S. 502, 508-518 (1917); *Keeler* v. *Standard Folding Bed Co.*, 157 U.S. 659, 666 (1895); *Hobbie* v. *Jennison*, 149 U.S. 355, 361-363 (1893); *Adams* v. *Burke*, 84 U.S. (17 Wall.) 453, 456 (1873).

Under this Court's cases, a patentee who sells an article embodying the invention (either directly or through an authorized licensee) cannot bring a patent-infringement suit against the purchasers for using the article for its only reasonable use or for reselling the article to others. See, *e.g.*, *Univis*, 316 U.S. at 250-252; *Motion Picture Patents*, 243 U.S. at 515-518; *Keeler*, 157

U.S. at 666; *Adams*, 84 U.S. (17 Wall.) at 456; *McQuewan*, 55 U.S. (14 How.) at 549-550. Instead, the enforceability of downstream restrictions after an authorized sale arises only "as a question of contract, and not as one under the inherent meaning and effect of the patent laws." *Keeler*, 157 U.S. at 666; accord *Motion Picture Patents*, 243 U.S. at 509, 513; *McQuewan*, 55 U.S. (14 How.) at 549-550.

This Court's cases treat the first-sale doctrine as "delimiting the scope of the patent grant." *Aro*, 377 U.S. at 497 (plurality opinion). As the Court has explained, "when the machine passes to the hands of the purchaser," it "passes outside" the scope of the patentee's rights, "and is no longer under the protection of the act of Congress." *McQuewan*, 55 U.S. (14 How.) at 549. Accord, *e.g.*, *United States* v. *General Elec. Co.*, 272 U.S. 476, 489 (1926); *Adams*, 84 U.S. (17 Wall.) at 456. In effect, an authorized sale of a patented article grants an implied-in-law license under patent law to practice the patent. See 35 U.S.C. 271(a) (use "without authority" constitutes infringement). As *Adams* explained, this Court's first-sale cases rest on the principle that "the sale by a person who has the full right to make, sell, and use such a machine *carries with it* the right to the use of that machine to the full extent to which it can be used." 84 U.S. (17 Wall.) at 455 (emphasis added); *Univis*, 316 U.S. at 249 (observing that an authorized sale is "both a complete transfer of ownership * * * and a license to practice" the patented invention).[2]

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[2] The Court has made clear, however, that a sale under a foreign patent in that foreign country does not exhaust the patent rights under the corresponding United States patent. See *Boesch* v. *Graff*, 133 U.S. 697 (1890).

The Court has drawn that limitation from the language of the statute: "all that [the patentee] obtains by the patent" is "the right to exclude every one from making, using, or vending the thing patented, without the permission of the patentee." *McQuewan*, 55 U.S. (14 How.) at 549; see, *e.g.*, *Motion Picture Patents*, 243 U.S. at 516. The Court has reasoned that once the patentee or authorized licensee validly parts with title to a machine embodying the patented invention, that sale, which could not lawfully be made without the patentee's authority, places that particular machine outside the exclusivity granted by the patent. After an authorized sale, a patentee is in a position no different from that of any inventor, with or without a patent, who lawfully passes title to a machine embodying his invention. *McQuewan*, 55 U.S. (14 How.) at 549. That is so, the Court has explained, because—unlike a licensee, who exercises a portion of the patentee's exclusive rights—one who purchases a patented article "for the purpose of using it in the ordinary pursuits of life * * * exercises no rights created by the act of Congress, nor does he derive title to [the machine] by virtue of the franchise or exclusive privilege granted to the patentee." *Ibid.* Once the patentee parts with title through an authorized sale, "[c]omplete title to the implement or machine purchased becomes vested in the vendee by the sale and purchase," *Mitchell* v. *Hawley*, 83 U.S. (16 Wall.) 544, 548 (1873), and the purchaser "becomes possessed of an absolute property in such articles, unrestricted in time or place," at least for patent-law purposes. *Keeler*, 157 U.S. at 666.

That long-standing construction of the patent statute is supported by the common law's historical hostility to servitudes on chattels. See *Straus* v. *Victor Talking Mach. Co.*, 243 U.S. 490, 500-501 (1917) (describing a

patentee's attempted downstream restrictions as "restraints upon [the property's] further alienation, such as have been hateful to the law from Lord Coke's day to ours, because obnoxious to the public interest"). Although patents have many of the attributes of personal property, 35 U.S.C. 261, and "the patentee may withhold his patent altogether from public use," the patent does not confer any right to sell the patented item burdened with ongoing restrictions of the patentee's choosing that are enforceable as a matter of patent law. *Motion Picture Patents*, 243 U.S. at 514, 516. That conclusion is supported by the same rationale underlying the common-law rule, namely, that public policy is best served by freedom of trade in chattels. *Keeler*, 157 U.S. at 667. Thus, whatever may be a patentee's right to enforce post-sale restrictions by way of contract law, the patentee (no more than any other property owner) has no property-like right to burden his invention with post-sale restrictions enforceable under *patent* law.[3]

This Court's cases also reflect that "the purpose of the patent law is fulfilled with respect to any particular

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[3] This Court has concluded that the state of the historical common law regarding restraints on alienation is irrelevant in the antitrust context, because "the Sherman Act's use of 'restraint of trade' 'invokes the common law itself, . . . not merely the static content that the common law had assigned to the term in 1890.'" *Leegin Creative Leather Prods., Inc.* v. *PSKS, Inc.*, 127 S. Ct. 2705, 2714 (2007) (citation omitted). That principle has no application in the patent context, where there is no comparable grant of authority and the meaning of the property-like statutory rights granted by Congress is, like other statutory grants, properly informed by the common-law understanding at the time of the original enactments. That is particularly true in light of Congress's re-codification of the relevant statutory language here without substantive change and without rejecting the previous judicial construction of the statute. See pp. 12-13, *infra*.

article when the patentee has received his reward for the use of his invention by the sale of the article, and * * * once that purpose is realized the patent law affords no basis for restraining the use and enjoyment of the thing sold." *Univis*, 316 U.S. at 251. The "reward" to which a patentee is entitled for a "machine or instrument whose sole value is in its use" is the compensation for which he (or one acting with his authority) first parts with title. *Hobbie*, 149 U.S. at 362. That is so because once the patentee has parted with title to a machine embodying his invention, he has no further rights under the patent laws in that machine. As this Court has explained, "as between the owner of a patent on the one side, and a purchaser of an article made under the patent on the other, the payment of a royalty once, or, what is the same thing, the purchase of the article from one authorized by the patentee to sell it, emancipates such article from any further subjection to the patent throughout the entire life of the patent." *Keeler*, 157 U.S. at 666.

Congress's re-enactment of the patent laws in 1952 supports this Court's construction of the statute. Acting against the backdrop of almost 100 years of this Court's precedents applying the first-sale doctrine to patent law, Congress made no effort to alter that construction. As this Court has recognized, "when 'judicial interpretations have settled the meaning of an existing statutory provision, repetition of the same language in a new statute indicates, as a general matter, the intent to incorporate its . . . judicial interpretations as well.'" *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Dabit*, 547 U.S. 71, 85 (2006) (citation omitted). That presumption is applicable here, where the only change that Congress made in the 1952 amendments to the grant of exclusive

rights was to change the text to "'the right to exclude others from making, using, or selling', following language used by the Supreme Court, to render the meaning clearer." S. Rep. No. 1979, 82d Cong., 2d Sess. 23 (1952); see *Deepsouth Packing Co.* v. *Laitram Corp.*, 406 U.S. 518, 531 (1972) ("We would require a clear and certain signal from Congress before approving the position of a litigant who * * * argues that the beachhead of privilege is wider, and the area of public use narrower, than courts had previously thought.").

The lone exception to this Court's treatment of the first-sale doctrine as delimiting the scope of the patent right was the short-lived decision in *Henry* v. *A.B. Dick Co.*, 224 U.S. 1 (1912), which was expressly overruled just five years later by *Motion Picture Patents*, 243 U.S. at 518. In allowing a patentee to remedy through the patent laws a violation of the requirement that pur-chasers could use its patented invention only with supplies purchased from the patentee, *A.B. Dick* read this Court's first-sale cases as recognizing only a license implied in *fact* to use the purchased article. 224 U.S. at 24. In so concluding, the *A.B. Dick* Court misread *Mitchell* as involving a conditional sale, see *id.* at 23, when, in fact, *Mitchell* involved an unauthorized sale, see 83 U.S. (16 Wall.) at 548-549. See pp. 16-17, *infra*.[4]

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[4] Respondent claims (Supp. Br. 7 n.4) that *A.B. Dick* retains force, but *Motion Picture Patents* expressly rejected the legal principle on which *A.B. Dick*'s holding rested, namely, "that, since the patentee may withold his patent altogether from public use he must logically and necessarily be permitted to impose any conditions which he chooses upon any use which he may allow of it." *Motion Picture Patents*, 243 U.S. at 514. The Court described that principle as "defect[ive]," *ibid.*, plainly rejected it, and accordingly concluded that it was "obvious" that "the decision in [*A.B. Dick*] must be regarded as overruled." *Id.* at 518.

The Court's decision in *Univis* confirms that the patent-exhaustion doctrine delimits the scope of the patent right, which cannot be extended or altered by the parties. In *Univis*, the Court rejected, as a defense to a Sherman Act claim, the argument that the patent statute authorized a maker of eyeglass lens blanks to impose resale-price restrictions on finished lenses made with the blanks.[5] The Court reasoned that the sale of the lens blanks by the patentee's authorized licensee "exhausts the monopoly in that article and the patentee may not thereafter, by virtue of his patent, control the use or disposition of the article." 316 U.S. at 250. Although the lens blanks did not themselves meet all the limitations of any of the patents until after the sale, when the downstream retailers processed them into finished lenses, the Court held that the first-sale doctrine still applied because the lens blanks were capable of use only in practicing the patents. *Id.* at 248-249; see *id.* at 249 (assuming that "each blank * * * embodies essential features of the patented device and is without utility until it is ground and polished as the finished lens of the patent").

In so holding, the Court reiterated the principle of its earlier cases, observing that "[t]he first vending of any article manufactured under a patent puts the article beyond the reach of the monopoly which that patent confers." *Univis*, 316 U.S. at 252. The Court also reasoned that "[a]n incident to the purchase of any article,

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[5] The Court's analysis of the failure of the patent-law defense survives the demise of the per se ban on resale-price maintenance. See *Leegin*, *supra*, overruling *Dr. Miles Med. Co.* v. *John D. Park & Sons Co.*, 220 U.S. 373 (1911). Indeed, properly understood, the first-sale doctrine continues to limit the scope of the patent defense and thereby allow courts to apply rule-of-reason analysis to resale-price-maintenance agreements involving patented goods.

whether patented or unpatented, is the right to use and sell it." *Id.* at 249. Thus, "[s]ale of a lens blank by the patentee or by his licensee is * * * in itself both a complete transfer of ownership of the blank, which is within the protection of the patent law, and a license to practice the final stage of the patent procedure." *Ibid.* The "license" to which the Court referred necessarily arose as a matter of law by virtue of the sale, and was not subject to alteration by the patentee, because it overrode the patentee's imposition of explicit restrictions purporting to limit the downstream finishers' right to sell the finished product. See *id.* at 243-246. If the implied license conferred by an authorized sale were merely a default rule that could be overridden by contrary statements of the patentee or agreement of the parties, the Court could not have found exhaustion in *Univis*.[6]

B. Under This Court's Cases, Patentees Can Remedy Violations Of Restrictions On Licensees By Means Of Patent-Infringement Suits Against Licensees And Those Who Knowingly Purchase In Unauthorized Sales

In contrast to the Court's consistent rejection of attempts by patentees to place patent-law limitations on use or resale by purchasers following authorized sales, this Court has repeatedly held that a patentee may require licensees to comply with any lawful restriction to which the parties may agree—including field-of-use re-

[6] This Court has never suggested that the patent-exhaustion doctrine applies to the *products* of a patented item that is capable of reproducing itself in the hands of the purchaser—*e.g.*, newly-grown seeds that are identical to, and grown from, a patented genetically-modified seed that was purchased from the patentee or an authorized licensee. See U.S. Amicus Br. at 14 & n.8, *McFarling* v. *Monsanto Co.*, 545 U.S. 1139 (2005) (No. 04-31). This case presents no opportunity to address that question.

strictions and even minimum-price restrictions—on pain of liability for patent infringement for both the licensee and purchasers with knowledge of the restriction. See, *e.g.*, *General Talking Pictures Corp.* v. *Western Elec. Co.*, 305 U.S. 124, 127 (1938); *General Elec.*, 272 U.S. at 489-490; *Mitchell*, 83 U.S. (16 Wall.) at 547-551. The Court has explained that licensees "stand[] on different ground" from purchasers in authorized sales, because a licensee holds a portion of the patentee's exclusive rights under the patent statute, whereas an article validly sold to a purchaser is "no longer within the limits of the monopoly." *McQuewan*, 55 U.S. (14 How.) at 549-550; see *Mitchell*, 83 U.S. (16 Wall.) at 548. Because the licensee stands in the shoes of the patentee, this Court generally has allowed the patentee to restrict its licensees as if the patentee itself were exercising the exclusive patent rights, as long as the restrictions "are normally and reasonably adapted to secure pecuniary reward for the patentee's monopoly." *General Elec.*, 272 U.S. at 490.

Among the license restrictions that, when breached, will give rise to a valid patent-infringement suit is a restriction on a licensee's ability to make an authorized sale. An early example is *Mitchell*, where the patentholders had conveyed to the licensee the right "*to license to others the right to use the [patented] machines*," 83 U.S. (16 Wall.) at 548 (quoting license), but had not conveyed to the licensee the right to sell the machines, and the license expressly forbade the licensee to "'*in any way, or form, dispose of, sell, or grant* any license to use the said machines beyond the expiration' of the original term." *Id.* at 549 (quoting license). Despite that license restriction, the licensee "sold" the machines to the defendants rather than merely licensing

their use. *Ibid.* When Congress extended the original patent term, the patent-holders brought a patent-infringement suit to enjoin the defendants' ongoing use of the machines. Notwithstanding the sale, *ibid.*, the Court held that the first-sale doctrine did not apply, because the seller "was only a licensee and *never had any power to sell a machine* so as to withdraw it indefinitely from the operation of the franchise secured by the patent," *id.* at 551 (emphasis added), making the sale unauthorized.[7]

More recently, in *General Talking Pictures*, the Court held that when a licensee sells a patented article in violation of the field-of-use terms of its license, "the effect is precisely the same as if no license whatsoever had been granted," and the patentee could sue both the licensee and the purchaser (who was on notice of the restriction) for infringement of the patent. 305 U.S. at 127. In *Univis*, by contrast, where the sale of the lens blanks was authorized (albeit expressly subject to limitations on resale), the patent-exhaustion doctrine applied, because "the authorized sale of an article which is capable of use only in practicing the patent is a relin-

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[7] Although, as respondent notes (Supp. Br. 6 & n.3), the Court in *Mitchell* referred to the fact that the licensee "sold" the machines, the Court never suggested that the licensee sold the machines within the scope of the authority granted him by the patent-holders. To the contrary, the Court's opinion emphasizes that the licensee did *not* have the authority to sell the machines, and the record in the case supports that conclusion. See Tr. of R. at 5-6, *Mitchell* v. *Hawley*, *supra* (No. 411) (Patentees "do hereby convey to the [licensee], the exclusive right to make and use, and to license to others the right to use, the said machines in the said States of Massachusetts and New Hampshire * * * during the remainder of the original term of said letters-patent. Provided that the [licensee] shall not in any way or form dispose of, sell, or grant any license to use the said machines, beyond the 3rd day of May, A. D. 1867.").

quishment of the patent monopoly with respect to the article sold." 316 U.S. at 249. The distinction between the rights of licensees and of authorized purchasers is thus a necessary and explicable result of the differences in their respective positions.

II. THE FEDERAL CIRCUIT'S UNDERSTANDING OF PATENT EXHAUSTION CANNOT BE RECONCILED WITH THIS COURT'S CASES

In recent years, the first-sale doctrine has evolved in the Federal Circuit in a manner that is materially different from the doctrine expounded by this Court. That evolution has downgraded this Court's substantive limitation on a patent owner's exclusive rights into a mere default rule that the patentee can override by placing "conditions" on the sale of his patented invention. That result is irreconcilable with the reasoning of this Court's patent-exhaustion cases.

A. In The Federal Circuit, The Patent-Exhaustion Doctrine Is Inapplicable To Explicit Post-Sale Restrictions

As the patent-exhaustion doctrine has evolved in the Federal Circuit, the doctrine "does not apply to an expressly conditional sale"—that is, to a sale that is subject to an express restriction on the right to use or to resell the patented invention. Pet. App. 5a (quoting *B. Braun Med., Inc.* v. *Abbott Labs.*, 124 F.3d 1419, 1426 (Fed. Cir. 1997)). The foundation of the Federal Circuit's approach to the first-sale doctrine is *Mallinckrodt, Inc.* v. *Medipart, Inc.*, 976 F.2d 700 (Fed. Cir. 1992). In *Mallinckrodt*, the patentee manufactured and sold to hospitals a medical device capable of reuse but marked with a "single use only" notice. *Id.* at 701. Many hospital-purchasers sent the used products to Medipart for reconditioning. *Ibid.* Under the reasoning of this

Court's first-sale cases, such a restriction on reuse, like an express restriction on resale, would be ineffective in an infringement action. The Federal Circuit, however, held that an otherwise valid "single use only" notice is enforceable in an action for patent infringement. *Id.* at 703-709.

The court of appeals construed this Court's patent-exhaustion cases as establishing only that "price-fixing and tying restrictions accompanying the sale of patented goods were *per se* illegal." *Mallinckrodt*, 976 F.2d at 704. In the court's view, this Court's cases "did not hold, and it did not follow, that all restrictions accompanying the sale of patented goods were deemed illegal." *Ibid.*; see *id.* at 708. Pointing to this Court's decision in *General Talking Pictures*, the court of appeals concluded that there was no persuasive basis for holding that "the enforceability of a restriction to a particular use is determined by whether the purchaser acquired the device from a manufacturing licensee or from a manufacturing patentee." *Id.* at 705.

The Federal Circuit thus rejects application of the first-sale doctrine to what it views as "conditional" sales, a category that evidently encompasses any sales subject to unilateral or bilateral restrictions on the use or resale of the purchased article. Pet. App. 4a-6a; *Mallinckrodt*, 976 F.2d at 706-708. As a result, a patentee may attach (by notice or agreement) restrictions on products embodying its patented invention and enforce those restrictions, in actions for patent infringement, against downstream purchasers even after an authorized sale by the patentee or a licensee. Pet. App. 6a. In the Federal Circuit's view, such restrictions are enforceable in patent-infringement suits unless the restriction is not "within the patent grant" (*i.e.*, does not "relate[] to subject mat-

ter within the scope of the patent claims"), has "anticompetitive effects extending beyond the patentee's statutory right to exclude," and violates antitrust law. *Mallinckrodt*, 976 F.2d at 708.

B. The Federal Circuit's Approach Is Inconsistent With This Court's Cases

The precedents of this Court foreclose the Federal Circuit's view that patent exhaustion is merely a default rule to be discarded whenever patentees choose to impose explicit restrictions on authorized purchasers' use or resale. Instead, this Court's cases make clear that the patent-exhaustion doctrine delimits the substantive scope of the patent grant. See pp. 8-15, *supra*. Indeed, this Court has repeatedly applied the patent-exhaustion doctrine in concluding that explicit restrictions imposed on authorized purchasers are ineffective as a matter of patent law. See, *e.g.*, *Univis*, 316 U.S. at 244, 249-252; *Boston Store* v. *American Graphophone Co.*, 246 U.S. 8, 25 (1918); *Motion Picture Patents*, 243 U.S. at 506-507, 516. The reasoning of those cases is irreconcilable with the Federal Circuit's treatment of patent exhaustion.

The court of appeals rests its contrary approach on a broad understanding of "conditional" sale, but that understanding is not reflected in this Court's cases. In *Mitchell*, the Court did allude to the notion of an unconditional sale, observing that the patent right is exhausted when the patentee "has himself constructed a machine and sold it without any conditions, or authorized another to construct, sell, and deliver it * * * without any conditions." 83 U.S. (16 Wall.) at 547; see *Keeler*, 157 U.S. at 663 (quoting the foregoing in describing *Mitchell*). But at that time, a "conditional" sale would have been understood as an agreement to sell

where title would not convey until performance of a condition precedent. See, *e.g.*, *Harkness* v. *Russell*, 118 U.S. 663, 666 (1886) (describing a "conditional sale" as a "mere agreement to sell upon a condition to be performed" in which title does not pass until the condition precedent is performed).[8]

That narrower understanding of "conditional" is consistent with this Court's other patent-exhaustion cases, which explain that the doctrine is triggered "if a person legally acquires a title to" a patented item (*Chaffee* v. *Boston Belting Co.*, 63 U.S. (22 How.) 217, 223 (1859)); when a patented item is "lawfully made and sold" (*Hobbie*, 149 U.S. at 363; *Adams*, 84 U.S. (17 Wall.) at 457) or "passes to the hands of the purchaser" (*McQuewan*, 55 U.S. (14 How.) at 549); or upon "the purchase of the article from one authorized by the patentee to sell it" (*Keeler*, 157 U.S. at 666). See *Motion Picture Patents*, 243 U.S. at 515-516 (describing as an "unconditional sale" a sale made subject to restrictions on resale price). Thus, under this Court's cases, if a purchaser acquires title to an item embodying the patented invention through a sale authorized by the patentee, the patent is exhausted—regardless of the patentee's purported imposition of an explicit restriction on use or resale.

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[8] Respondent suggests (Supp. Br. 6 & n.3) that *Mitchell* involved "conditione*d*" sales, and that that concept is somehow different from "conditional." The Court in *Mitchell*, however, used neither of those terms, speaking instead of sales "without conditions." See 83 U.S. (16 Wall.) at 548. Courts in that era used the terms "conditional" and "condition" in relation to sales interchangeably. See, *e.g.*, *William W. Bierce, Ltd.* v. *Hutchins*, 205 U.S. 340, 345-347 (1907) (noting that sale of property purported to make "the passing of title * * * subject to a condition precedent," and deciding that "the sale was conditional"); *Harkness*, 118 U.S. at 666.

This Court's decision in *Univis* confirms that understanding, because the Court relied on the first-sale doctrine in concluding that explicit post-sale restrictions were not within the scope of the patent grant. The Federal Circuit misreads *Univis* as standing only for the proposition that restrictions that have been found to be unlawful restraints on trade in the patent context, such as "price-fixing or tying" arrangements, cannot be enforced in a patent-infringement suit. See *Mallinckrodt*, 976 F.2d at 708; Resp. Supp. Br. 5-8. But that reading gives too little weight to the critical first step of the Court's analysis in *Univis*. The lawsuit in *Univis* was an action under the Sherman Act. But before considering whether the defendants' conduct violated antitrust law, the Court first asked whether that conduct was "excluded by the patent monopoly from the operation of the Sherman Act." 316 U.S. at 243. And to answer that question (*i.e.*, to determine whether the defendants' conduct was within the scope of the patent grant, and thus immune from antitrust scrutiny), the Court looked to the patent-exhaustion doctrine. Only after concluding that the authorized sales had exhausted the patentee's rights under the patent law did the Court analyze the antitrust claims. See *id.* at 251 (because of the first-sale doctrine, the "stipulation by the patentee fixing resale prices derive[d] no support from the patent" and was placed "on the same footing under the Sherman Act as like stipulations with respect to unpatented commodities"). Although the antitrust claim was the catalyst for the Court's analysis of the patent-exhaustion doctrine in *Univis*, the Court's resulting substantive patent-law holding has force as a definitive construction of the patent law even in infringement actions that are unrelated to any antitrust claims.

The test adopted by the Federal Circuit in *Mallinckrodt* thus reflects a fundamental misunderstanding of the role and scope of the patent-exhaustion doctrine. According to *Mallinckrodt*, the first step in determining the validity of an explicit use or resale restriction is to determine whether it is "within the patent grant," and if it is, "that ends the inquiry." 976 F.2d at 708. But the Federal Circuit bars consideration of patent-exhaustion principles in making that initial determination, whereas *Univis* and other decisions of this Court make clear that the first-sale doctrine delimits the scope of the patentee's patent-law rights and therefore *must* be considered in determining whether a particular post-sale restriction is "within the patent grant." The court of appeals' approach cannot be reconciled with those precedents.

This Court's reasoning in *Univis* also refutes the Federal Circuit's reliance on *General Talking Pictures*. See *Mallinckrodt*, 976 F.2d at 705. In *Univis*, this Court refused to reconsider the very distinction that the Federal Circuit has jettisoned, namely, the distinction between restrictions placed on licensees (which are effective under the patent laws against knowing purchasers after unauthorized sales) and restrictions placed on purchasers after an authorized sale (which are not). See 316 U.S. at 252 (distinguishing *General Electric* and noting that the Court there "was at pains to point out that a patentee who manufactures the product protected by the patent and fails to retain his ownership in it can not control the price at which it is sold by his distributors"). As explained below, there are substantial reasons to retain this Court's latter rule, and no need to address in this case whether the former should be reconsidered. There are limits on what can be accomplished

through a valid license and so there is no reason that the treatment of licensees and purchasers needs to be co-extensive.

Finally, the Federal Circuit's view (evidenced most clearly by the decision below) that patentee-imposed use restrictions are generally enforceable against authorized purchasers as a matter of patent law cannot be reconciled with this Court's frequent suggestion that whether a patentee can place enforceable downstream restrictions following an authorized sale turns on contract, not patent, law. See, *e.g.*, *Keeler*, 157 U.S. at 666; *McQuewan*, 55 U.S. (14 How.) at 549-550. The Federal Circuit glosses over that distinction, observing that "[t]he question whether a license restriction is binding on the purchaser is indeed one of contract law," but that "the remedy for breach of a binding license provision is not exclusively in contract," but also through suits for patent infringement. *Mallinckrodt*, 976 F.2d at 707 n.6. If that were so, this Court's observations to the contrary in cases rejecting claims under the patent law would make little sense. See *Motion Picture Patents*, 243 U.S. at 509; *Keeler*, 157 U.S. at 666; *McQuewan*, 55 U.S. (14 How.) at 549-550. Thus, although the Federal Circuit has correctly recognized that not "all restrictions accompanying the sale of patented goods [a]re deemed illegal," *Mallinckrodt*, 976 F.2d at 704, the court errs in concluding that any downstream restriction that does not "violate[] some other law or policy" therefore can be enforced under the *patent* law. *Id.* at 708.[9]

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[9] Respondent suggests (Supp. Br. 8 & n.5) that *Keeler*'s reference to the patentee's potential ability to protect himself by "special contracts," 157 U.S. at 666, does not preclude enforcement of such contracts by means of patent law. But that strained reading of *Keeler* was rejected by the Court in *Motion Picture Patents*, which confirmed that "[t]he

C. Method Patents Should Be Subject To The Same Patent-Exhaustion Doctrine As Other Patents

The court below held (Pet. App. 6a) that method patents are categorically exempt from the operation of the first-sale doctrine. Scant rationale, however, has been offered for that conclusion. See *Bandag, Inc.* v. *Al Bolser's Tire Stores, Inc.*, 750 F.2d 903, 924 (Fed. Cir. 1984) (concluding that patent-exhaustion doctrine was inapplicable "because the claims of the Carver patent are directed to a 'method of retreading' and cannot read on the equipment Bolser used in its cold process recapping"); *Glass Equip. Dev., Inc.* v. *Besten, Inc.*, 174 F.3d 1337, 1341 n.1 (Fed. Cir. 1999) (stating conclusion).

Although this Court has never directly addressed the question, some of its patent-exhaustion cases have involved method patents, and the Court has never suggested that such patents are categorically exempt from the exhaustion doctrine. See, *e.g.*, *Dawson Chem. Co.* v. *Rohm & Haas Co.*, 448 U.S. 176, 186 (1980) (accepting concession that the patentee's sale of a chemical specially suited for use in a patented method exhausts the

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extent to which the use of the patented machine may validly be restricted to specific supplies *or otherwise by special contract* between the owner of a patent and the purchaser" is "a question *outside the patent law*." 243 U.S. at 509 (emphases added) (citing *Keeler*). Accord *McQuewan*, 55 U.S. at 549-550 (after an authorized sale, the patented article "is no longer under the protection of the act of Congress," and "[c]ontracts in relation to it are regulated by the laws of the State, and are subject to State jurisdiction"). Respondent also asserts that *Hobbie* supports a contrary view, because it states that "[i]t is easy for a patentee to protect himself" by "tak[ing] care to bind every licensee or assignee, if he gives him the right to sell articles made under the patent, by imposing conditions." 149 U.S. at 363. But that statement merely confirms that the Court treats restrictions on licensees differently from purported restrictions on authorized purchasers.

patentee's method patent, and citing *Univis* and *Adams*); *General Elec.*, 272 U.S. at 480, 490 (finding no exhaustion); see also *Leitch Mfg. Co.* v. *Barber Co.*, 302 U.S. 458, 461 (1938) (noting, where patentee sells unpatented bituminous emulsion to road builders for use in practicing patented but unlicensed method, that "whenever such a sale is made, the law implies authority to practice the invention"). Indeed, if method patents were never subject to exhaustion upon an authorized sale of an article whose only reasonable use is to practice the patented method, it would be easy in many circumstances to avoid the patent-exhaustion doctrine simply by applying for a method patent in conjunction with a machine, manufacture, or composition patent. Cf. *Bandag*, 750 F.2d at 922 (noting that it "is commonplace that the claims defining some inventions can by competent draftsmanship be directed to either a method or an apparatus"). There is no evident reason why the patent-exhaustion doctrine should be deemed inapplicable to method patents.

III. THE COURT SHOULD REAFFIRM ITS LONG-STANDING INTERPRETATION OF THE PATENT-EXHAUSTION DOCTRINE

Not only is the Federal Circuit's patent-exhaustion doctrine irreconcilable with the reasoning of this Court's cases, there is no valid reason for this Court to follow the Federal Circuit's lead in diluting that long-established doctrine, and much reason not to do so.

This Court's patent-exhaustion decisions long ago provided sound doctrinal bases for the doctrine, see pp. 8-15, *supra*, resting on the language and purpose of the patent laws, and those bases remain sound. Indeed, the doctrinal foundation of the rule has only been strength-

ened by Congress's re-enactment of the patent laws. See pp. 12-13, *supra*. The Court has said less about the practical policy reasons for the doctrine, viewing "[t]he inconvenience and annoyance to the public" if the law were otherwise "too obvious to require illustration." *Keeler*, 157 U.S. at 667.

This case provides an illustration. Absent patent exhaustion, the lawful purchase of an article useful only for practicing the patent provides no value to the purchaser until completion of further negotiations and a further payment for the right to use or to resell. Moreover, the need for further negotiations and payments may depend on a court's after-the-fact determination whether the seller adequately expressed a limitation on the rights conveyed. Compare Pet. App. 59a (district court holding that notice required by respondent was "not sufficient to transform" sale by Intel "into a conditional one"), with *id.* at 6a (Federal Circuit holding that the sales to petitioners were conditional, without exploring which of them received notice or when). The potential for "inconvenience and annoyance," as well as inefficiency, is palpable.

That potential is not limited to the first purchaser. If the patentee can impose use and resale restrictions on the first purchaser in an authorized sale, there is no reason why it cannot also do so as to all subsequent purchasers. Here, for example, respondent (having already received a royalty from Intel) could also extract royalties not only from petitioners, but also from customers who purchase computers from petitioners for resale, on pain of infringement liability. The inconvenience, annoyance, and inefficiency can thus be passed down the

chain of distribution, with no obvious stopping point short of the end of the article's useful life.[10]

That ability to employ the patent law to extract royalties at multiple downstream points in the channels of commerce, even after an authorized sale, can have consequences beyond the evident transactional inefficiencies. As amici have observed, a patentee's negotiating leverage downstream is not necessarily reduced by the amount of the royalties it obtained from upstream licensees. Dell Br. 9-11; see generally FTC, *To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy* Ch. 2, at 29 (Oct. 2003) <http://www.ftc.gov/os/2003/10/innovationrpt.pdf> ("If a[] * * * producer learns that it has infringed a patent only after it has committed sunk costs to its * * * production—and thus locked in to the effort—the patentee may be in a position to demand supra-competitive royalty rates."). The result would be a transfer of wealth from downstream firms and ultimate consumers to the patentee. Nothing suggests that this transfer would further "the Progress of Science and useful Arts," U.S. Const. Art. I, § 8, Cl. 8, to the benefit of the public. At least since the decision in *Keeler*, this Court has adhered to the view that the right to place such downstream restrictions should be resolved as a matter of

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[10] Although suits by a patentee against ultimate retail consumers might be unlikely as a practical matter, suits by patentees against their competitors, or others, for direct or contributory infringement would not be. See, *e.g.*, *Motion Picture Patents*, 243 U.S. at 507-508 (patentee sued, *inter alia*, a movie manufacturing company and a movie supplier for making and supplying films for use on patented film projector in violation of post-sale restrictions); *Mallinckrodt*, 976 F.2d at 701 (patentee sued company that was refurbishing patented medical device for patentee's customers, who were violating patentee's "single use" restriction).

contract, not patent, law. See 157 U.S. at 666-667; *Motion Picture Patents*, 243 U.S. at 509, 513, 515.

The Federal Circuit's approach also has the potential to erode downstream competition by permitting patentees to avoid antitrust scrutiny of restrictions on the use and resale of products embodying their inventions—restrictions that would be within the scope of the patent grant (and thus, in the Federal Circuit's view, immune from antitrust scrutiny). *Mallinckrodt* concedes that some post-sale restrictions may be invalid because they violate the antitrust laws—but limits that concession to restrictions not "reasonably within the patent grant," *i.e.*, restrictions unrelated "to subject matter within the scope of the patent claims." 976 F.2d at 708. The ambiguity of that criterion (and the court's rejection of the first-sale doctrine as an enforceable limitation on the scope of the patent grant) may permit potentially anticompetitive post-sale restrictions on reuse, repair, or servicing to escape antitrust scrutiny. Moreover, the court's analysis appears to get matters backwards (restrictions are not outside the patent grant because they violate the antitrust laws, rather restrictions that might otherwise violate the antitrust laws may be immunized if they are within the patent grant), and at a minimum is ambiguous and confusing.

Some of the same restrictions that the first-sale doctrine renders ineffective in a patent-infringement suit could be validly imposed as a matter of state contract law. But even otherwise valid contract provisions would not provide a defense to a federal antitrust action, and mere unilateral notice to downstream purchasers will not generally give rise to enforceable contractual restrictions. Moreover, manufacturers may not be in privity of contract with potential competitors that would

provide substantially more attractive targets for lawsuits than the manufacturer's own direct customers. Cf. n.10, *supra*. Patent law should not be read to grant more extensive rights.

Finally, "there is an argument for [retaining the Court's long-standing patent-exhaustion doctrine] on the basis of *stare decisis* alone." *Leegin Creative Leather Prods., Inc.* v. *PSKS, Inc.*, 127 S. Ct. 2705, 2720 (2007). That argument is particularly powerful here. In *Leegin*, the Court departed from the rule of *stare decisis* because of compelling considerations unique to the antitrust precedent it overruled and to the special status of the Sherman Act in the courts. *Id.* at 2720-2725. In contrast, the record here reveals no considerations favoring a departure from *stare decisis*—and the government is aware of none. Indeed, respondent has not argued to date that this Court should depart from its settled doctrine, but rather has insisted (albeit incorrectly) that the Federal Circuit has accurately construed that doctrine.

IV. THE JUDGMENT SHOULD BE VACATED AND THE CASE REMANDED

The judgment below rests on the same erroneous understanding of patent exhaustion that infuses the Federal Circuit's approach to this area of the law. Although the court recognized that "Intel was free to sell its microprocessors and chipsets" to petitioners (Pet. App. 6a), the court nevertheless held that respondent could impose, and enforce by way of a patent-infringement suit, restrictions on the rights of purchasers to whom title passed. That holding is incorrect.

The court of appeals did not address whether, absent what it found to be enforceable "conditions" on the sale,

Intel's authorized sale of the components would exhaust the patents at issue. The sale here was not of an article covered by those patents, see Pet. App. 3a, but rather merely of a component of the patented systems and methods. See Br. in Opp. 3-4. Although *Univis* held that an authorized sale of an article exhausts relevant patents if the article "embodies essential features" of the patented invention and "is capable of use only in practicing the patent," 316 U.S. at 248-249,[11] that case did not precisely delineate the required relationship between the purchased article and the patented invention. Under the logic of *Univis*, if the article sold by or with authorization from the patentee is especially made or adapted for infringing the patentee's patent(s), constitutes a material part of the invention, and has no substantial noninfringing use—in short, if the unauthorized sale of the article would constitute contributory infringement, as the Court assumed was true in *Univis*, *id.* at 249—an authorized sale should exhaust the patentee's ability to assert infringement of such patent(s) against the purchaser. Cf. 35 U.S.C. 271(c). Here, the district court held that respondent's system patents were exhausted, based on its conclusion that Intel's chips and microprocessors were "'destined . . . to be finished by the purchaser in conformity'" to respondent's system patents, and have "no reasonable non-infringing use." Pet. App. 55a. The court of appeals, however, did not address that question, so a remand for consideration of that issue would be appropriate.

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[11] The Court also spoke of the relationship as one in which the patentee "has destined the article to be finished by the purchaser in conformity to the patent," *Univis*, 316 U.S. at 251, or has sold it "for the purpose of enabling the buyer to finish and sell it." *Id.* at 252.

CONCLUSION

The judgment of the court of appeals should be vacated and the case remanded for further proceedings.

Respectfully submitted.

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